Description of Costing Methodology for Realignment Analysis

1. The VISNs used the Market Plan submitted in April as the starting point. Workload was static, amount of space at each site was static, and neither could be changed. The VISN used the IBM Market Planning Template. The local in-house unit costs and local contract unit costs for managing the workload, and the local construction unit costs were all developed nationally, and could not be "changed" in the database by the VISN. (The VISNs could elect to "adjust" these, as explained later.)

2. The VISNs then developed 1-3 alternatives, or scenarios for the realignment as required by VACO. These would be closing a campus, reducing a campus to an 8-hour operation, etc. *(Also Reference the document labeled Cost Definitions)* The steps to develop the alternatives were as follows:

   Automatic Cost Calculations:

   a. For each type of care (Medicine beds, Primary Care, etc), the VISN would first determine **where** the workload would be managed. (This would involve transferring workload to and from different facilities as required)
   b. Then the VISN would determine **how** the workload would be managed at each site of care (This would involved determining workload to be managed in-house, by contract, by sharing agreement, etc.)
   c. The cost for managing the workload is then calculated automatically based on where the workload is managed and how it is managed. (Workload units x cost/unit = total cost for workload)
   d. After the amount of workload to be managed in-house is determined, the amount of space required is automatically calculated. The new space requirement is compared to the existing space at the facility, and the **excess space** is then called "vacant", and if the site is **short on space**, the VISN had to add new space by new construction, converting vacant, leasing space, etc.
   e. The construction and/or lease costs are calculated automatically, based on square feet and location.
   f. The VISN continues this through all the categories of care. Then the VISN determines Admin space and Research space using a suggested formula. Again, excess space is then called "vacant", and if additional space is needed, the VISN added the space by construction or lease.
   g. The costs for Admin and Research are calculated automatically based on a cost per square foot. (Personnel costs are already included in the in-house costs for managing the workload.)

h. The VISN determines how to manage the remaining vacant space with demolition, divestiture, enhanced use, or remaining vacant.
i. The costs for maintaining vacant space are automatically calculated, as well as the demolition costs, or the sale of the property.

VISN Identified Costs/Savings

a. In each category of care, the VISN could elect to identify additional savings or costs not calculated automatically by IBM. These would be entered in the appropriate year(s) by the VISN. (On the realignment spreadsheets these are the line items in Step 5 labeled "Savings/Costs/Profits", and you would find these under "Recurring Costs", "Recurring Savings" or "Non-Recurring Savings". These would include, but not limited to:
    i. Additional construction costs for seismic or hazardous materials.
    ii. Additional or reduced transportation costs
    iii. Adjusting the in-house costs if the VISN was a cost outlier and anticipated reducing or increasing the in-house costs.
    iv. Adjusting the contract costs if the VISN believed that the contract costs paid locally was higher or lower than the number determined nationally (based on Medicare).
    v. Parking construction or leases
    vi. Potential Enhanced Use Revenue
    vii. Lease revenue
    viii. Land Acquisition
    ix. Other costs and savings

3. When the VISN completes the steps above, for each alternative, the Life Cycle Costs are then calculated for each Alternative, including the existing Market Plan and Status Quo. As explained in the document titled "Cost Definitions", the Life Cycle Cost is the sum of the discounted costs and savings over the life cycle (in our case from 2004-2022). Discounted costs are calculated using the OMB inflation and discount rates – the 2001 current costs are inflated by 1.9%/year and then discounted back to Present Value at a rate of 5.3%/year. All costs in the Realignment Analysis documents are presented in Present Value, or "Discounted".

4. The Life Cycle Costs were then compared for all scenarios/alternatives and the Market Plan and Status Quo. The DIFFERENCE between the alternative and the Market Plan demonstrates the additional savings or costs that can be expected if the facility was realigned.

Frequently Asked Questions:

1. Why does the analysis show more facilities than just the one being studied for realignment? With workload transferring between facilities, the best way to capture the additional savings and costs for the realignment alternatives was to show the total costs for all the facilities involved (transferring and receiving facilities) in all the scenarios, and then comparing them. This ensures that we are comparing like scenarios with equal workload.

2. **Why does the 100% contract option show construction costs?** This is a 3 part answer:
    a. If the facility was only asked to study a conversion to an 8-hour operation, then they are NOT contracting out 100% of the workload, only the Inpatient component. Therefore, the construction needed for the remaining services would stay in the plan.
    b. If the construction costs were at a "receiving facility", then chances are that the costs were already planned in the original Market Plan and the Realignment didn't change the need for these.

3. **Why does construction show up at the receiving facilities, even in the options where they are not receiving any new workload?** If you look at the original Market Plan and compare the construction costs, they should then be the same. You will want to note any differences between the original Market Plan and the alternative to determine what is directly related to the realignment alterative.

4. **Why do the construction costs in the later years look low compared to what I think they should be?** All the costs in the Realignment Analysis are Discounted or Present Value dollars. This means that we started with actual 2001 costs, and then inflated them each year by the OMB Inflation rate of 1.9% and then discounted them each year by the OMB discount rate of 5.3% a year. So, a construction project that may have cost $5 Million in 2001 would show up in 2008 as discounted as $ 3.9 Million.

5. **How were the in house costs determined?** The in-house costs were determined using the facility DSS costs which included:

    - Fixed Indirect Costs (~36% of total cost): Includes fiscal, Director's office, engineering, M&R, NRM, leases, housekeeping, etc. These were adjusted to eliminate any national overhead items.

- Fixed Direct Costs (~7% of total cost): Includes ward clerks, office supplies and administrative support.
- Variable Costs (~57% of total cost): Includes direct patient care costs, nursing staff, physicians, medical supplies, etc.

6. **How were the contract costs determined?** The contract costs were determined and provided by the contractor CACI and were based on local Medicare costs.

7. **Why don't I see any specific staffing savings?** The staff costs are included in the in-house costs, so they follow the workload trend. When transferring the workload to other facilities, the in-house costs at the transferring facility will go down, and the in-house costs at the receiving facility will go up. With the economy of scale, in most cases the amount of costs going up at the receiving station should be less than the initial costs at the transferring facility.

8. **How were the construction and lease costs determined?** The professional estimators in the VHA Office of Facilities provided these unit costs. These were based on locality and type of construction. These unit costs were then multiplied by the square footage for the new construction or renovation.

9. **How was the revenue from Enhanced Use determined?** The VISN determined this amount, using the contractor's (AEW) assessment as a guideline. In many cases, the value was amortized over 30 years to determine an annual amount expected in revenue.